Coachman Insurance Company

2004

ANNUAL REPORT

Responsibility for Financial Statements

105-04307/

The financial statements are the responsibility of management and have been prepared in conformity with accounting principles generally accepted in Canada. In the opinion of management, the financial statements fairly reflect the financial position, results of operations and cash flows of Coachman Insurance Company (the Corporation) within reasonable limits of materiality.

Preparation of financial information is an integral part of management's broader responsibilities for the ongoing operations of the Corporation. Management maintains an extensive system of internal accounting controls to ensure that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial statements.

An actuary has been appointed by the Corporation to carry out a valuation of the policy liabilities and to issue a report thereon to the shareholders and regulatory authorities. The valuation is carried out in accordance with accepted actuarial practice and common Canadian insurance regulatory requirements. The policy liabilities consist of a provision for unpaid claim and adjustment expenses on the earned portion of policies and of future obligations on the unearned portion of policies. In performing this valuation, the actuary makes assumptions as to future rates of claim frequency and severity, inflation, reinsurance recoveries, expenses and other contingencies, taking into consideration the circumstances of the Corporation and the nature of the insurance policies. The actuary also makes use of management information provided by the Corporation and the work of the external auditors in verifying the data used in the valuation.

The financial statements have been examined and approved by the Board of Directors. An Audit and Finance Committee, composed of members of the Board of Directors, meets periodically with financial officers of the Corporation and the external auditors. These external auditors have free access to this Committee, without management present, to discuss the results of their audit work and their opinion on the adequacy of internal financial controls and the quality of financial reporting.

KPMG LLP have been appointed external auditors. Their responsibility is to report to the shareholders and regulatory authorities regarding the fairness of presentation of the Corporation's financial position and results of operations as shown in the consolidated financial statements. In carrying out their audit, the external auditors also make use of the work of the actuary and his report on the policy liabilities. The Auditors' Report outlines the scope of their examination and their opinion.

Jon Schubert
President

Don Thompson
Chief Financial Officer

February 22, 2005

Actuary's Report

To the Shareholders of the Coachman Insurance Company

I have valued the policy liabilities of Coachman Insurance Company for its statement of financial position at December 31, 2004 and their change in the statement of operations and deficit for the year then ended in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of policy liabilities makes appropriate provision for all policyholder obligations, and the financial statements fairly present the results of the valuation.

Richard Gauthier
Fellow, Canadian Institute of Actuaries

February 22, 2005

Auditors' Report

To the Shareholders of Coachman Insurance Company

We have audited the statement of financial position of Coachman Insurance Company as at December 31, 2004 and the statements of operations and deficit and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants
Regina, Canada

February 22, 2005

Statement of Financial Position

December 31	2004	2003
	(thousands of $)	
Assets		
Cash and cash equivalents (note 3)	$ 3,296	$ 2,719
Accounts receivable (notes 4 & 15)	10,120	11,037
Deferred policy acquisition costs	2,082	1,689
Reinsurers' share of unearned premiums (note 7)	1,654	1,543
Future income taxes (note 10)	4,771	827
Investments (note 5)	59,956	52,022
Unpaid claims recoverable from reinsurers (notes 7 & 8)	29,323	17,776
Property, plant and equipment (note 6)	56	81
	$ 111,258	$ 87,694
Liabilities		
Accounts payable	$ 1,283	$ 1,704
Premium taxes payable	199	407
Future income taxes (note 10)	4,771	827
Amounts due to reinsurers (note 7)	2,587	2,475
Unearned reinsurance commissions	42	30
Unearned premiums (note 15)	10,766	10,056
Provision for unpaid claims (notes 8 & 15)	80,460	61,727
	100,108	77,226
Shareholders' equity		
Share capital (note 11)	1,000	1,000
Contributed surplus	25,600	25,600
Deficit	(15,450)	(16,132)
	11,150	10,468
	$ 111,258	$ 87,694

Commitments (note 16)

(see accompanying notes)

Statement of Operations and Deficit

year ended December 31	2004	2003
	(thousands of $)	
Gross premiums written	$ 32,475	$ 24,294
Net premiums written	$ 29,129	$ 19,784
Net premiums earned (note 7)	**$ 27,866**	$ 28,432
Claims incurred (note 7)	24,542	24,979
Commissions (note 7)	4,581	2,895
Administrative expenses	2,303	2,477
Premium taxes (note 7)	956	951
Facility Association participation (note 15)	(737)	1,275
Total claims and expenses	**31,645**	32,577
Underwriting loss	**(3,779)**	(4,145)
Investment earnings (note 9)	4,333	4,466
Income before income taxes	**554**	321
Income tax recovery (note 10)	128	–
Net income	**682**	321
Deficit, beginning of year	(16,132)	(16,453)
Deficit, end of year	**$ (15,450)**	$ (16,132)

(see accompanying notes)

Statement of Cash Flows

year ended December 31	2004	2003
	(thousands of $)	
Cash provided by (used for):		
Operating activities		
Net income	$ 682	$ 321
Non-cash items:		
Realized gain on disposal of investments	(1,393)	(1,813)
Amortization	415	392
Change in non-cash operating items (note 12)	7,804	2,467
	7,508	1,367
Investing activities		
Purchase of investments	(102,699)	(96,286)
Proceeds on sale of investments	95,788	85,703
Purchase of property, plant and equipment	(20)	–
	(6,931)	(10,583)
Financing activities		
Contributed surplus	–	9,400
Increase in cash and cash equivalents	**577**	184
Cash and cash equivalents, beginning of year	2,719	2,535
Cash and cash equivalents, end of year	**$ 3,296**	$ 2,719

(see accompanying notes)

Notes to the Financial Statements

December 31, 2004

1. STATUS OF THE CORPORATION

Coachman Insurance Company (the "Corporation") was incorporated under the laws of Ontario on June 12, 1979. The Corporation holds an Ontario provincial insurer's licence under *The Ontario Insurance Act* and is licensed to conduct business in Ontario.

2. SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The following are considered to be significant:

Deferred policy acquisition costs

Premium taxes, commissions and certain underwriting and policy issuance costs are charged to expenses over the term of the insurance policies to which they relate. The method followed in determining the deferred policy acquisition costs limits the amount of the deferral to the amount recoverable from unearned premiums after giving consideration to investment income, as well as claim and adjustment expenses expected to be incurred as the premiums are earned.

Investments

Bonds and debentures are recorded at amortized cost. Treasury bills are recorded at cost. Gains and losses on the disposal of investments are taken into income on their trade date. Investments are written down when there is a decline in value that is other than temporary.

Provision for unpaid claims

The provision for unpaid claims represents an estimate of the total cost of outstanding claims to the year-end date. Included in the estimate are reported claims, claims incurred but not reported and an estimate of adjustment expenses to be incurred on these claims. The provision is calculated using discounting. The estimates are necessarily subject to uncertainty and are selected from a range of possible outcomes. During the life of the claim, adjustments to the estimates are made as additional information becomes available. The change in outstanding losses plus paid losses is reported as claims incurred in the current period.

Premiums

Premiums written are recognized as revenue evenly over the terms of the related policies. Unearned premiums represent the portion of premiums written relating to the unexpired terms of policies in force.

Reinsurance ceded

Reinsurance premiums ceded and reinsurance recoveries on losses incurred are recorded as reductions of the respective income and expense accounts.

Unpaid claims recoverable from reinsurers are estimated in a manner consistent with the method used for determining the provision for unpaid claims.

Property, plant and equipment
Property, plant and equipment are recorded at cost less accumulated amortization. Amortization is recorded on a straight-line basis, commencing in the year in which the asset is placed in service, over the estimated useful lives of the assets as follows:

Computer hardware, system costs and other equipment	20 – 33$^1/_3$%

Income taxes
The Corporation uses the asset and liability method of accounting for income taxes. Current income taxes are recognized as estimated income taxes payable for the current year. Future income tax assets and liabilities consist of temporary differences between tax and accounting bases of assets and liabilities as well as the benefit of losses available to be carried forward to future years for tax purposes that are likely to be realized. The effect on future tax assets and liabilities of a change in tax rates is recognized as income in the period that includes the date of enactment or substantive enactment. A valuation allowance is recorded against any future income tax asset if it is more likely than not that the asset will not be realized.

Cash and cash equivalents
Cash and cash equivalents consist of cash on hand and treasury bills with a maturity of 90 days or less from the date of acquisition.

Measurement uncertainty
The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and changes in estimates are recorded in the accounting period in which they are determined. The most significant estimation process is related to the actuarial determination of the provision for unpaid claims (note 8).

3. CASH AND CASH EQUIVALENTS

Cash and cash equivalents include $2,720,000 (2003 - $2,990,000) in treasury bills earning an average effective interest rate of 2.5% (2003 – 2.7%).

4. ACCOUNTS RECEIVABLE

	2004	2003
	(thousands of $)	
Financed premiums receivable	$ 4,415	$ 4,078
Facility Association receivable	2,013	2,334
Due from reinsurers	1,445	2,513
Due from self-insured retentions	1,157	1,275
Accrued investment income	546	404
Other	336	214
Due from brokers	208	219
Total accounts receivable	$ 10,120	$ 11,037

5. INVESTMENTS

The carrying value and fair value of the Corporation's investments are as follows:

	2004		2003	
	(thousands of $)			
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Short-term investments	$ 4,102	$ 4,102	$ 3,578	$ 3,578
Bonds and debentures	55,854	56,232	48,444	48,955
Total investments	$ 59,956	$ 60,334	$ 52,022	$ 52,533

Details of significant terms and conditions, exposures to interest rate and credit risks of investments are as follows:

(i) Short-term investments:

Short-term investments are comprised of treasury bills with a maturity of less than one year but greater than 90 days from the date of acquisition. These investments have an average effective interest rate of 2.6% (2003 – 2.9%) and an average remaining term to maturity of 90 days (2003 - 129 days). The Corporation's investment policy states that investments must meet minimum investment standards of R-1, as rated by a recognized credit rating service.

Carrying amounts for short-term investments approximate fair value due to the immediate or short-term nature of these financial instruments.

(ii) Bonds and debentures:

The Corporation's investment policy states that the minimum quality standard for purchase of bonds and debentures is A, as rated by a recognized credit rating service.

The Corporation's investment policy limits its holdings for any one issuer, other than Government of Canada bonds, provincial bonds and their guarantees, to 5% of the market value of the total portfolio.

The carrying value and average effective interest rates are shown below by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers have the right to call or prepay obligations with or without call or prepayment penalties. The carrying values are essentially the same as the principal values and therefore the average effective rates are not materially different from the coupon rates. Interest is generally payable on a semi-annual basis.

	2004		2003	
	(thousands of $)			
Term to maturity (years)	Carrying Value	Average Effective Rates	Carrying Value	Average Effective Rates
Government of Canada:				
One or less	$ 50	6.5%	$ 50	6.5%
After one through five	18,224	4.5%	10,297	3.8%
After five	12,725	4.6%	16,580	5.1%
Canadian provincial and municipal:				
After one through five	6,426	5.0%	4,306	5.9%
After five	5,473	5.7%	6,838	5.8%
Canadian corporate:				
After one through five	8,366	4.8%	5,431	5.0%
After five	4,590	5.2%	4,942	5.7%
Total bonds and debentures	$ 55,854		$ 48,444	

For bonds and debentures, the fair values are considered to approximate quoted market values on recognized stock exchanges, based on the latest bid prices.

Investments with a carrying value of $50,000 are on deposit with regulatory authorities as at Dec. 31, 2004. Investments with a carrying value of $650,000 are on deposit with a bank for a loan facility with respect to overdraft protection.

6. PROPERTY, PLANT AND EQUIPMENT

The components of the Corporation's investment in property, plant and equipment, as well as related amortization is as follows:

	2004			2003
	(thousands of $)			
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Computer hardware, system costs and other equipment	$ 765	$ 709	$ 56	$ 81

Amortization for the year is $45,000 (2003 - $98,000).

7. REINSURANCE CEDED

The Corporation has reinsurance treaties with SGI CANADA and other third party reinsurers, which limits the liability of the Corporation to a maximum amount on any one loss as follows:

	(thousands of $)
General liability and property	$ 150
Automobile	250
Catastrophe	250

The following table sets out the amount by which reinsurance ceded has reduced the premiums earned, claims incurred and commissions and premium taxes:

	2004	2003
	(thousands of $)	
Premiums earned	$ 3,234	$ 2,995
Claims incurred	14,550	6,693
Commissions and premium taxes	96	58

8. PROVISION FOR UNPAID CLAIMS

(i) Nature of unpaid claims:

The establishment of the provision for unpaid claims is based on known facts and interpretation of circumstances and is therefore a complex process influenced by a large variety of factors. Measurement of the provision is uncertain due to claims that are not reported to the Corporation at the year-end date and therefore estimates are made as to the value of these claims. As well, uncertainty exists for reported claims that have not been settled, as all the necessary information may not be available at the statement of financial position date.

Factors used to estimate the provision include: the Corporation's experience with similar cases, historical trends involving claim payments, the characteristics of the class of business, claim severity and claim frequency, the effect of inflation on future claim settlement costs, court decisions and economic conditions. Time is also a critical factor in determining the provision, since the longer it takes to settle and pay a claim the more variable the ultimate settlement amount will be. Accordingly, short-tail claims such as physical damage or collision claims tend to be more reasonably predictable than long-tail claims such as liability claims.

As a result, the establishment of the provision for unpaid claims relies on a number of factors and on the judgment and opinions of a large number of individuals, which necessarily involves risk that the actual results may differ materially from the estimates.

Changes in the estimates for the provision for unpaid claims are as follows:

	2004	2003
	(thousands of $)	
Net unpaid claims – beginning of year	$ 43,951	$ 40,210
Provision for self-insured retention	(1,275)	(1,285)
Payments made during the year relating to prior year claims	(11,366)	(13,190)
Deficiency relating to prior year estimated unpaid claims	3,255	2,370
Net unpaid for claims of prior years	34,565	28,105
Provision for claims occurring in the current year	15,415	14,571
Provision for self-insured retention	1,157	1,275
Net unpaid claims – end of year	$ 51,137	$ 43,951

The fair value of the provision for unpaid claims and unpaid claims recoverable from reinsurers has been omitted because it is not practicable to determine fair value with sufficient reliability.

(ii) Type of unpaid claims:

The provision for unpaid claims is summarized by type of claim as follows:

	2004			2003		
	(thousands of $)					
	Gross	Reinsurance Recoverable	Net	Gross	Reinsurance Recoverable	Net
Automobile	$ 76,981	$ 28,912	$ 48,069	$ 59,911	$ 17,671	$ 42,240
Property	1,563	389	1,174	415	105	310
Liability	759	22	737	126	–	126
Self-insured retention	1,157	–	1,157	1,275	–	1,275
Total	$ 80,460	$ 29,323	$ 51,137	$ 61,727	$ 17,776	$ 43,951

(iii) Self-insured retention:

The provision for self-insured retention represents unpaid claim reserves associated with insurance policies where the insured is retaining the insurance risk. The Corporation holds security in the form of deposits in custodial accounts to guarantee the reserves associated with the self-insured retention policies.

(iv) Structured settlements:

During the normal course of settling insurance claims, the Corporation has purchased annuities from life insurance companies to make fixed payments to claimants of the Corporation. There are no rights under the non-commutable, non-assignable, non-transferable contracts that would provide for any current or future benefit to the Corporation. The Corporation remains liable only in the event that the life insurance company fails to make payments to the Corporation's claimant. As at Dec. 31, 2004, no information has come to the Corporation's attention that would suggest any weakness or failure in the life insurance companies from which it has purchased the annuities. Consequently, no provision for the credit risk is required. The net present value of these expected payments as of the statement of financial position date total $1,780,000 (2003 - $676,000).

9. INVESTMENT EARNINGS

The components of investment earnings are as follows:

	2004	2003
	(thousands of $)	
Income from interest	$ 2,287	$ 2,192
Realized gain on sale of investments	1,393	1,813
Income from premium financing	653	402
Income from dividends	–	59
Total investment earnings	$ 4,333	$ 4,466

10. INCOME TAXES

Income tax expense differs from the amount that would be computed by applying the federal and provincial statutory income tax rates to income before income taxes. The reasons for the differences are as follows:

	2004	2003
	(thousands of $)	
Net income before income taxes	$ 554	$ 321
Combined federal and provincial tax rate	36.12%	36.62%
Computed tax expense based on combined rate	$ 200	$ 118
Increase (decrease) resulting from:		
Investment earnings not subject to taxation	–	(22)
Adjustment to future tax assets and liabilities for enacted changes in tax laws and rates	–	1,093
Valuation allowance	(283)	(1,218)
Other	(45)	29
Total income tax recovery	$ (128)	$ –

The components of future income tax balances are as follows:

	2004	2003
	(thousands of $)	
Future income tax assets		
Provision for unpaid claims	$ 8,927	$ 1,192
Unearned premiums	3,889	–
Tax loss carryforward	–	7,963
Other	30	30
	12,846	9,185
Less: valuation allowance	(8,075)	(8,358)
Total future income tax assets	4,771	827
Future income tax liabilities		
Unpaid claims recoverable from reinsurers	3,301	321
Bonds and debentures	873	506
Reinsurers' share of unearned premiums	597	–
Total future income tax liabilities	4,771	827
Net future income taxes	$ –	$ –

11. SHARE CAPITAL

The Corporation is authorized to issue 10,000 common shares. At the end of 2004 there are 10,000 (2003 – 10,000) common shares issued.

12. CHANGE IN NON-CASH OPERATING ITEMS

The change in non-cash operating items is comprised of the following:

	2004	2003
	(thousands of $)	
Accounts receivable	$ 917	$ 3,925
Deferred policy acquisition costs	(393)	(747)
Reinsurers' share of unearned premiums	(111)	(1,149)
Unpaid claims recoverable from reinsurers	(11,547)	(2,951)
Accounts payable	(421)	340
Premium taxes payable	(208)	153
Amounts due to reinsurers	112	1,965
Unearned reinsurance commissions	12	30
Unearned premiums	710	(5,791)
Provision for unpaid claims	18,733	6,692
	$ 7,804	$ 2,467

13. FAIR VALUE

The fair value of financial assets and liabilities, other than investments (note 5), unpaid claims and unpaid claims recoverable from reinsurers (note 8) approximate fair value due to their immediate or short-term nature.

14. RELATED PARTY TRANSACTIONS

Included in these financial statements are transactions with various Saskatchewan Crown corporations, departments, agencies, boards and commissions related to the Corporation by virtue of common control by the Government of Saskatchewan and non-Crown corporations and enterprises subject to joint control and significant influence by the Government of Saskatchewan (collectively referred to as "related parties"). Routine operating transactions with related parties are settled at prevailing market prices under normal trade terms.

Transactions and amounts outstanding at year end are as follows:

Category	2004	2003
	(thousands of $)	
Investments	$ 474	$ 463
Accounts receivable	2	2
Accounts payable	–	37
Investment earnings	55	47

SGI CANADA provides management and administrative services to the Corporation as well as being one of its reinsurers (note 7). Administrative expenses incurred by SGI CANADA and charged to the Corporation were $885,000 (2003 - $531,000) and accounts payable are $159,000 (2003 - $322,000).

In 2003, the Corporation entered into an agreement with SGI CANADA, the Corporation's ultimate majority shareholder, whereby SGI CANADA would transfer to the Corporation, net amounts recoverable after Dec. 31, 2002 on reinsurance for adverse loss development on Coachman losses occurring prior to April 30, 2001. The Corporation will reimburse SGI CANADA for any costs it may incur under the reinsurance contract. At Dec. 31, 2004, $2,293,000 (2003 - $1,945,000) was accrued under this reinsurance policy and has reduced claims incurred.

Other related party transactions are disclosed separately in the notes to the financial statements.

15. FACILITY ASSOCIATION

The Corporation is a participant in various automobile risk sharing pools in Ontario, whereby companies in the industry share resources to provide insurance coverage to high risk insureds.

Facility Association transactions recorded in the Corporation's financial results are as follows:

	2004	2003
	(thousands of $)	
Gross premiums written	$ 771	$ 2,733
Net premiums earned	$ 1,437	$ 1,807
Claims incurred	582	2,659
Commissions	(45)	134
Premium taxes	43	54
Administrative expenses	201	291
Total claims and expenses	781	3,138
Underwriting profit (loss)	656	(1,331)
Investment earnings	81	56
Net income (loss)	$ 737	$ (1,275)
Facility Association receivable	$ 2,013	$ 2,334
Unearned premiums	557	1,223
Provision for unpaid claims	2,660	3,071

16. COMMITMENTS

The Corporation has a lease for its office premises expiring Dec. 31, 2008 at an annual rent of $180,000.

17. COMPARATIVE FINANCIAL INFORMATION

For comparative purposes, certain 2003 balances have been reclassified to conform to 2004 financial statement presentation.

Coachman